Supp. 35; *Oertel v. Glenn*, 13 Fed. Supp. 651; *Utah Oil Refining Company v. Hinchley*, ... F. (2d) ..... (CCA 10).

d. The Third Circuit Court of Appeals has said—"We think that these capital stock tax cases are ad valorem taxes • • • ." *American Viscose Corporation v. Rothensies*, ... F. (2d) ..... If that were true, the tax would be unconstitutional because it is not apportioned according to population.

3. It is highly desirable that this Court determine the true nature of the capital stock tax and the constitutionality thereof in connection with *Scaife & Co. v. Commissioner*, where on June 2, 1941, this Court granted certiorari. That case involves the question as to whether an amended capital stock tax return may be filed after the expiration of the filing date. There are also pending in this Court the petitions for rehearing of General Motors Corporation and United Motor Service, Inc. (Nos. 738, 739) on denial of petitions for Writs of Certiorari. These involve the same question as that presented in this petition.

BRIEF IN SUPPORT OF PETITION

Reference to the opinion below, jurisdiction, a statement of the questions presented, facts in the cases, specifications of errors to be urged, and reasons for granting the writ, will be found in the foregoing petition. The statutes involved are set out in the Appendix, *infra*, pp. 16-19.

SUMMARY OF STATUTES

These cases involve the constitutionality of Sections 215 of the National Industrial Recovery Act and 701 of the Revenue Act of 1934. The former was adopted on June 16, 1933, the latter on May 10, 1934. Both sections impose an excise tax upon a corporate taxpayer with respect to doing business for any part of the year ending June 30, 1933 and 1934, respectively, of $1 for each $1,000 of the adjusted declared value of its capital stock. Said section 215 exempted any corporation which did not do business during a part of the period from the date of the enactment of the National Industrial Recovery Act (June 16, 1933) to June 30, 1933, and said section 701 exempted any corporation which did not do business during a part of the period from the date of the enactment of the Revenue Act of 1934 (May 10, 1934) to June 30, 1934. These sections require the filing of returns for the first year, making a declaration of the value of a corporation's capital stock—and provide that such declared value may not be amended. For all subsequent years the adjusted declared value was to be the original declared value after making certain specified capital adjustments.

Sections 216 and 702 of said Acts, respectively, impose for each income taxable year ending after the close of the first capital stock tax year, an excess-profits tax equivalent to 5 per centum of the corporation's income as was in excess of 12½ per centum of the adjusted declared value, determined as aforesaid.

Section 703 of the Revenue Act of 1934 limited the application of Section 215 of the National Industrial Recovery Act to the year ending June 30, 1933.

ARGUMENT

"This Court has recognized that a statute purporting to tax may be so arbitrary and capricious as to amount to confiscation and offend the Fifth Amendment." *Nichols v. Coolidge*, 274 U.S. 531.

Assuming that the Acts in question require declarations of value of capital stock having some reasonable relation to fair value, we submit that there is no reasonable basis or standard for determining a value or capital stock for all time, as required by these Acts. A value declared under Section 215 of the National Industrial Recovery Act and 701 of the Revenue Act of 1934 was binding upon the taxpayer for all time. A value for capital stock as determined in 1933 may be fair and reasonable at that time, but may be wholly arbitrary, unreasonable and unfair in 1934 and subsequent years. The financial and economic history of this country during the last ten years is ample proof of this statement. The financial history of these petitioners as set out in the record filed herein further sustains it.

The capital adjustments required by said Acts have no reasonable relation to value and may readily run counter to changes in value. Distribution of earnings and profits under the statutes reduces the values as declared, whereas, it is apparent that regular dividend distributions by a corporation tend to increase the market value of its shares of stock. In the case of the petitioner, Prime Securities Corporation, the corporation made a declaration of value of $1,974,000.00, based on a net worth of the corporation as of December 31, 1932, using the market value of its assets. In 1933 the corporation sold a part of these assets.

Because of the statutory provision requiring the corporation to use the transferor's costs in determining the taxable gain thereon, the corporation secured a taxable gain of over a million dollars. While there was practically no change in the market value of the assets of the corporation, under the capital stock tax provisions, its declared value would be increased by over a million dollars. Many other examples of the same nature could readily be shown.

The privilege given by subsequent Congressional enactments to change the declaration of value made conclusively binding for all time in prior Acts does not render such prior Acts reasonable and constitutional. On the contrary, it is to some extent a recognition by Congress of the unreasonable nature of the requirements of such prior Acts.

> "The taxpayer may justly demand to know when and how he becomes liable for taxes. He cannot foresee and ought not to be required to guess the outcome of pending measures." *Untermeyer v. Anderson,* 276 U.S. 440.

Any declaration of value for all time cannot be based upon any of the underlying factors which the Courts have held must be taken into consideration in determining the value of the capital stock.

> "But the value of property results from the use to which it is put and varies with the profitableness of that use, present and prospective, actual and anticipated. There is no pecuniary value outside of that which results from such use." *Cleveland, Cincinnati, Chicago and St. Louis Ry. Co. v. Backus,* 154 U.S. 439.

Any declaration of value for all time cannot possibly have any reasonable relationship to any known or accepted

standard for determining value and a tax imposed on such declaration of value is not only so unreasonable and arbitrary as to be violative of the Fifth Amendment, but is also a direct tax imposed in violation of Art. I, Sec. 2, Subd. 3, and Art. I, Sec. 9, Subd. 4 of the Constitution of the United States. *Levy v. Wardell,* 258 U.S. 542.

Assume, however, that the statute does not intend that the taxpayer make a declaration having any reasonable relationship to actual value, and that the Acts in question permit the taxpayer to declare any value for its capital stock regardless of actual or fair value. In that situation, the capital stock tax provisions in question are unconstitutional because together with the excess-profits tax they compel the taxpayer to guess the future trend of its earnings for all time. The financial history of the petitioners, as disclosed by the record filed herein and the financial and economic history of this country, of which the Court will take judicial notice, show the utter impossibility of determining with any reasonable degree of accuracy, the trend of future earnings.

Judge Hamilton, now sitting in the Sixth Circuit Court and who concurred in the result only in these cases, in his opinion as District Judge in *Oertel v. Glenn,* 13 F. Supp. 651, said:

> "If the Act here in question (capital stock tax) is construed to raise a conclusive presumption that the tax is to be levied on the declared value of the taxpayer regardless of the actual value, it is violative of the Fifth Amendment."

The unreasonable nature of the Acts is disclosed by the facts in the cases here presented and especially by

the case of petitioner, Prime Securities Corporation. There the corporation made a declaration of value based on the market value of its assets. Shortly after the declaration, the corporation was compelled to sell a large block of stock in order to pay off its bank loans. By reason of the income tax provisions, this corporation was required to use the transferor's cost for the stock which it sold, resulting in a taxable gain of over a million dollars. Despite the fact that it made a declaration of value in accordance with market value of assets which the sale did not change, the Commissioner asserted a deficiency of over $57,000.00 of excess-profits tax against this corporation.

The necessity for raising revenue, preventing tax avoidance or the difficulty of administration, do not justify deprivation of constitutional rights. *Schlessinger v. Wisconsin,* 270 U.S. 230; *Heiner v. Donnan,* 285 U.S. 312.

RETROACTIVE FEATURES OF THE TAX

Under Section of the N. I. R. A., a corporation which was engaged in business during the entire period from July 1, 1932 to June 15, 1933, and ceased doing business on the latter date, was not liable for any tax for the year ending June 30, 1933, whereas, a corporation which was organized and started doing business on June 30, 1933, was subject to the tax for the entire year.

Under Section 701 of the Revenue Act of 1934, a corporation which did business during the entire period from July 1, 1933 to May 9, 1934, and ceased doing business on May 9, 1934, whereas, a corporation which was organized

and started doing business on June 30, 1934, was subject to the tax for the entire tax year. A period of sixteen days in one instance, and fifty days in the other, is by Congress declared to be a taxable year. We submit that the unreasonable, arbitrary and discriminatory nature of the retroactive provisions of the Act here in question, and the long period of retroactivity, render them unconstitutional. It is to be noted that the previous capital stock tax repealed in 1926 was applied prospectively and granted no discriminatory and unreasonable exemptions.

In *Hudson v. U.S.*, 12 F. Supp. 620; 13 F. Supp. 640, the Court of Claims in considering the question of the constitutionality of the "Silver Purchase Act" as an excise tax, said:

> "We think, putting these decisions together, it may be said that they hold in effect that if at the time a citizen enters into a transaction it is not taxable and he has no reason to believe or expect a tax will in the future be imposed by reason of it, a valid tax thereon cannot be laid by subsequent Statute."

While this Court on appeal upheld the constitutionality of this Act, it did not deny the validity of the principal as thus stated by the Court of Claims. It sustained the Act on the ground that it imposed "a special income tax", and that the period of retroactivity (35 days) was not unreasonable. *U.S. v. Hudson*, 299 U.S. 498. See also, *Nichols v. Coolidge*, 274 U. S. 531.

The retroactive application of the capital stock tax also destroys the character of the tax as one on privileges and so renders it invalid as an unapportioned direct tax for-

bidden by Sections 2 and 9 of Article I of the Constitution. *Milliken v. U.S.*, 283 U.S. 15; *Levy v. Wardell*, 258 U.S. 542.

WHEREFORE, it is respectfully submitted that this petition for Writs of Certiorari to review the judgments of the United States Circuit Court of Appeals for the Sixth Circuit should be granted.

BENJAMIN E. JAFFE,
Attorney for Petitioners,
2406 Fisher Building,
Detroit, Michigan.